William F. Adler
Executive Director
Federal Regulatory Relations

1275 Pennsylvania Avenue, N.W., Suite 400
Washington, D.C. 20004
(202) 383-6435

PACIFIC TELESIS
Group-Washington

December 30, 1993

RECEIVED

DEC 3 0 1993

FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

DOCKET FILE COPY ORIGINAL

William F. Caton
Acting Secretary
Federal Communications Commission
Mail Stop 1170
1919 M Street, N.W., Room 222
Washington, D.C. 20554

Dear Mr. Caton:

Re: *RM 8388 - Inquiry Into Policies and Programs to Assure Universal Telephone Service in a Competitive Market Environment*

On behalf of Pacific Bell and Nevada Bell, please find enclosed an original and six copies of their "*Reply Comments*" in the above proceeding.

Please stamp and return the provided copy to confirm your receipt. Please contact me should you have any questions or require additional information concerning this matter.

Sincerely,

William F. Adler /KD

Enclosures

No. of Copies rec'd 0+5
List A B C D E

RECEIVED

DEC 30 1993

FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, DC 20554

In the Matter of Inquiry into Policies and Programs to Assure Universal Telephone Service in a Competitive Market Environment	)	RM 8388

REPLY COMMENTS OF PACIFIC BELL AND NEVADA BELL

Pursuant to the Public Notice dated November 16, 1993, Pacific Bell and Nevada Bell hereby file reply comments on the petition of MFS Communications Co., Inc. ("MFS") for a Notice of Inquiry ("NOI") and En Banc Hearing with respect to universal service issues.

We support in principle MFS's request for a proceeding to identify the subsidies implicit in existing telecommunications pricing and to determine what subsidies, if any, should take their place. Today's rules incorporate a vast and intricate system of subsidies that was premised on the absence of local exchange competition and on a definition of "universal service" that has not been revisited since the Great Depression. The comments display wide differences of opinion on such basic questions as what universal service is or should be, what a subsidy is, and the fairest way to eliminate subsidies or achieve universal service. It is, in short, even more daunting than MFS lets on. That should not deter the Commission from taking action. The Commission's own decisions have made action critical.

There would be no point in responding to every contention made in the comments with which we disagree. We think reform should proceed in accordance with the following principles.

1. Expanded interconnection for switched transport and special access, open network architecture, exponential declines in the costs of both switching and mass transport technologies, the explosive growth of cellular telephone service and the rapid emergence of other alternatives to landline service such as PCS, and the smashing of boundaries between traditionally separate businesses and types of common carriage (such as radio, wireline, and cable TV), have made nearly every service we provide subject to competition now or in the immediate future. The monopoly premise for the current rules is obsolete.

The nature of our burden is different from the ones borne by most businesses. Millions of customers will continue to rely on us as the carrier of last resort. Our provision of service to those customers has been kept afloat by revenues from the very services that are now subject to competition. As those revenues are threatened, the cost of remaining on the network for everyone else rises. It is not just a matter for LEC shareowners to worry about.

2. The current rules have done a good job in the past of ensuring the availability of basic telephone service to nearly everyone who wants it. But left unaltered, the current system of

subsidies, non-cost-based rates, and efficiency penalties (such as the price cap sharing mechanism) will be a future disincentive to the universal deployment of more advanced services such as broadband. If the rules continue to handicap us or any other providers, the network of the future may still be built but it will not be built efficiently or ubiquitously. Consumers will pay billions more in rates for the network of the future than they have to, and some consumers may not have access to it at all.

3. In markets where no one provider has market power, regulation is not only unjustified but almost always contrary to the public interest. The only legal restrictions that are justified in competitive markets are the principles of the antitrust laws. Practically nothing that we provide is an essential facility anymore. Wisely, the antitrust laws generally do not control behavior by prematurely intervening in markets and handicapping some market participants but not others. It should come as no surprise that erecting redundant "safeguards" on the most efficient carriers results in huge and unjustified efficiency losses that are borne by consumers. The Commission's greatest successes have resulted from decisions to refrain from regulating competitive businesses, such as CPE, cellular, and LEC billing and collection service. In every one of these instances costs fell, prices fell, and consumer choices increased, all without any apparent anticompetitive activities by the incumbent players.

"Regulated competition" is an oxymoron. Regulation mimics the political process, not the market process. It is a forum in which producers and distributors are well represented but consumers are not. Regulation does not foster competition -- only, at times, a plethora of inefficient competitors, and that is not the same thing.

4. The current systems of separations and subsidies cannot be sustained under competition. Our access prices are not cost-based now, and the current rules do not allow us to move them toward cost anytime soon. The end user common line charge (EUCL) reduced the subsidy on transport somewhat, but a huge subsidy remains. In addition, the separations rules overstate the interstate portion of our fixed costs -- another way to avoid recovering loop costs in loop charges.

The subsidies embedded in our rates are the eight hundred pound gorilla of "managed competition." They are far too massive to be absorbed by shareholders (and regardless of size, there is no good reason shareholders should have to absorb them). Like consumers, shareholders have choices and will invest their money elsewhere. No new business opportunity will offset the loss of present subsidies. They are not attributable to plant that is no longer necessary or useful or to wrongheaded investment decisions. They are costs that regulators obligated us to incur to provide universal service.

If the Commission tries to "manage" such subsidies as it did before customers had choices, it will continue to encourage bypass and therefore threaten universal service by increasing the cost burden on customers who remain. If the LECs are not allowed to recover their joint and common costs in a rational and efficient way, the subsidies will be halted in the most destabilizing way possible: customers with choices will just stop buying access services that are laden with subsidies, implicit or explicit. It will be tempting to deal only with the explicit subsidies. That is flawed because it ignores the way that markets operate. The real legacy of our universal service obligations -- the subsidy that customers avoid paying when they have a choice -- is not just explicit support flows but the entire contribution above long-run incremental cost from services such as transport to fixed costs such as the loop. Buyers with competitive choices will avoid services that are priced above the market whether the reason for the above-market price is an implicit or an explicit subsidy.

The following roadmap suggests itself. The Commission should proceed by means of a Notice of Inquiry, clarifying the issues to be decided in a subsequent rulemaking, but it should proceed rapidly. Since reform of the separations rules will be required, a joint board will have to be convened. Reform of the access charge rules that keep rates for competitive services well above long-run incremental costs should not await separations reform, however. It is a short-term imperative to preserve universal service as it is.

Respectfully submitted,

PACIFIC BELL
NEVADA BELL

John W. Bogy

JAMES P. TUTHILL
JOHN W. BOGY
BETSY S. GRANGER

140 New Montgomery St., Rm. 1523
San Francisco, California 94105
(415) 542-7634

JAMES L. WURTZ

1275 Pennsylvania Avenue, N.W.
Washington, D.C. 20004
(202) 383-6472

Their Attorneys

Date: December 30, 1993

CERTIFICATE OF SERVICE

I, D. E. Van Laak, hereby certify that copies of the foregoing "REPLY COMMENTS OF PACIFIC BELL AND NEVADA BELL" re RM 8388 Petition of MFS Communications for a NOI and En Banc Heraings, were served by hand or by first-class United States mail, postage prepaid, upon the parties appearing on the attached service list this 30th day of December, 1993.

By: D. E. Van Laak

D. E. Van Laak

PACIFIC BELL
140 New Montgomery Street
San Francisco, California 94105

RM 8388
0559B

Service List

William F. Caton *
Acting Secretary
Federal Communications Commission
1919 M St., N.W., Rm. 222
Washington, D.C. 20554

International Transcription Service *
1919 M St., N.W., Rm. 246
Washington, D.C. 20554

Kathleen B. Levitz *
Acting Chief, Common Carrier Bureau
Federal Communications Commission
1919 M St., N.W., Rm. 500
Washington, D.C. 20554

Andrew D. Lipman
Russell M. Blau
Swidler & Berlin
3000 K St., N.W.
Washington, D.C. 20007

J. Manning Lee
Attorney for Teleport Comm. Group
1 Teleport Dr., Ste. 301
Staten Island, NY 10311

Bradley Stillman
Attorney for Consumer Fed. of America
1424 16th St., N.W., Ste. 604
Washington, D.C. 20036

Laurie J. Bennett
Attorney for US West
1020 19th St., N.W.
Washington, D.C. 20036

Robert M. Lynch
Attorney for Southwestern Bell
One Bell Center, Rm. 3520
St. Louis, MO 63101

M. Robert Sutherland
Attorney for BellSouth
4300 Southern Bell Center
Atlanta, GA 30375

Michael F. Hydock
Attorney for MCI
1801 Pennsylvania Ave., N.W
Washington, D.C. 20006

Lawrence W. Katz
Attorney for Bell Atlantic
1710 H St., N.W.
Washington, D.C. 20006

Martin T. McCue
VP/Gen. Counsel - USTA
1401 H St., N.W., Ste. 600
Washington, D.C. 20005

Francine J. Berry
Attorney for AT&T
295 North Maple Ave., Rm. 3244J1
Basking Ridge, NJ 07920

Gail L. Polivy
Attorney for GTE
1850 M St., N.W., Ste. 1200
Washington, D.C. 20036

Thomas J. Moorman
Attorney for John Staurulakis, Inc.
6315 Seabrook Rd
Seabrook, MD 20706

W. Theodore Pierson, Jr.
Attorney for Local Telecomm. Svcs.
1200 19th St., N.W., Ste. 607
Washington, D.C. 20036

* Service By Hand

0559B

John T. Lenahan
Attorney for Ameritech
2000 W. Ameritech Center Dr, Rm 4H86.
Hoffman Estates, IL 60196-1025

Kathy L. Shobert
Attorney for General Communications
888 16th St., N.W., Ste. 600
Washington, D.C. 20006

Edward E. Niefoff
Attorney for NYNEX
120 Bloomingdale Rd.
White Plains, NY 10605

Joanne Salvatore Bochis
Attorney for NECA
100 S. Jefferson Rd.
Whippany, NJ 07981

Daniel L. Brenner
Attorney for NCTA
1724 Massachusetts Ave., N.W.
Washington, D.C. 20036

Margot Smiley Humphrey
Attorney for Nat'l Rural Telecom
1150 Connecticut Ave., N.W., Ste. 1000
Washington, D.C. 20036

Ellen S. Deutsch
Attorney for Citizens Utility Co.
P.O.Box 340
8920 Emerald Park Dr., Ste. C
Elk Grove, CA 95759-0340

Michael J. Shortley, III
Attorney for Rochester Telephone
180 South Clinton Ave.
Rochester, NY 14646

Lawrence P. Keller
Director-Cathey, Hutton & Assoc.
3300 Holcomb Bridge Rd., Ste. 286
Norcross, GA 30092

Darrell S. Townsley
Attorney for Illinois Commerce Comm.
160 N. LaSalle St., Ste. C-800
Chicago, IL 60601

Lisa M. Zaina
Attorney for OPASTCO
21 Dupont Circle, N.W., Ste. 700
Washington, D.C. 20036

Jonathon E. Canis
Attorney for Coalition of Midwestern
Competitive Access Providers
3000 K St., N.W., Ste. 300
Washington, D.C. 20007

H. Richard Juhnke
Attorney for Sprint Corp.
1850 M St., N.W., 11th Floor
Washington, D.C. 20036

Brian R. Moir
Attorney for ICA
1255 23rd St., N.W., Ste. 800
Washington, D.C. 20037-1170

Leonard J. Kennedy
Attorney for Hyperion Telecomm.
1255 23rd St., Ste. 500
Washington, D.C. 20037

Susan McAdams
AVP for Electric Lightwave, Inc.
8100 NE Parkway Dr., Ste. 200
Vancouver, WA 98662

Dr. Barbara O'Connor
Chair-Alliance for Public Technology
901 15th St., Ste. 230
P.O. Box 28578
Washington, D.C. 20005-2301